

Economic and Revenue Forecast

Presented to
Local Government Partnership Meeting

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Summary

- The economic outlook has weakened since June
 - The recovery is expected to be painfully slow
 - Historical data has been revised downward
 - Risk of double-dip is higher, but unlikely
- Mostly due to the weaker economic outlook, revenue collections for the current and next biennia have been reduced by a total of \$1.44 billion

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The worst recession since WW II ended in June 2009

Recession	Peak-to-trough decline		Recession Duration
	Real GDP	Employment	
	<i>percent</i>	<i>percent</i>	<i>months</i>
1948-49	1.6	5.0	11
1953-54	2.5	3.4	10
1957-58	3.1	4.2	8
1960-61	0.5	2.3	10
1969-70	0.2	1.2	11
1973-75	3.2	1.9	16
1980	2.2	2.3	6
1981-82	2.6	3.1	16
1990-91	1.4	1.4	8
2001	0.7	1.7	8
Average	1.8	2.6	10
2007-09	4.1	6.1	18

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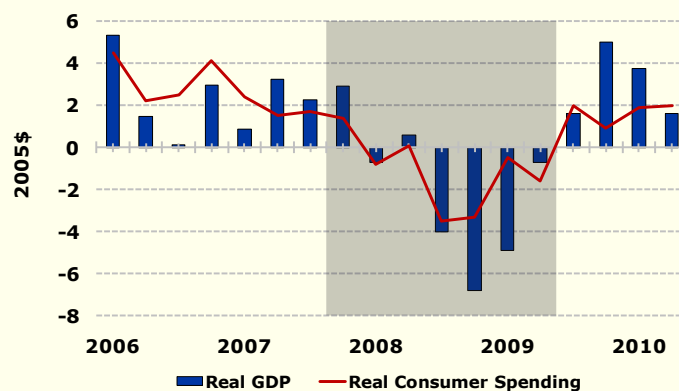
Source: NBER, ERFC

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GDP growth took off in 2009Q4 and 2010Q1 but then slowed

Percent growth, SAAR



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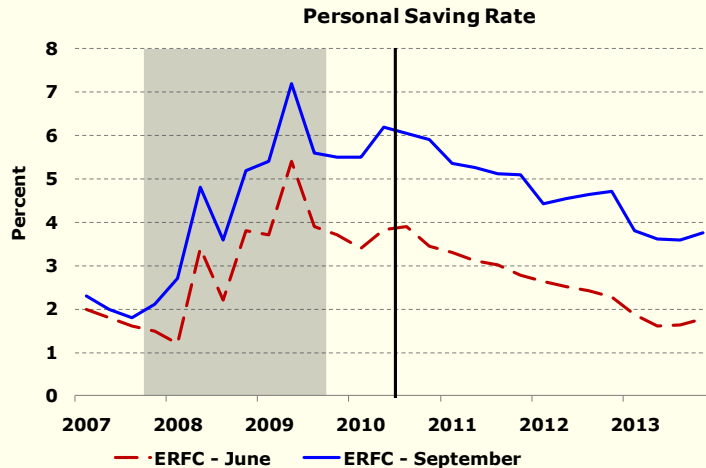
Source: BEA, data through 2010 Q2

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The historical savings rate was revised up sharply, affecting our forecast

The saving rate for 2010Q1 was revised from 3.1% of disposable income to 5.5%.



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Source: ERFC September 2010 forecast; actual through 2010 Q2

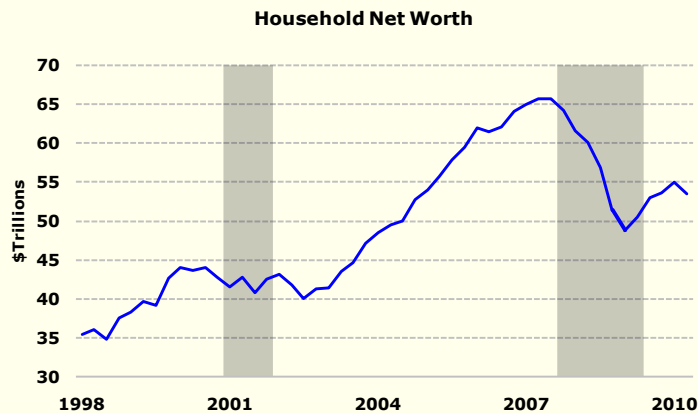
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Recovery in household net worth stalled in 2010Q2

\$18 trillion of wealth was lost in this recession

\$6 trillion has been recovered so far



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Source: Federal Reserve; data through 2010 Q2

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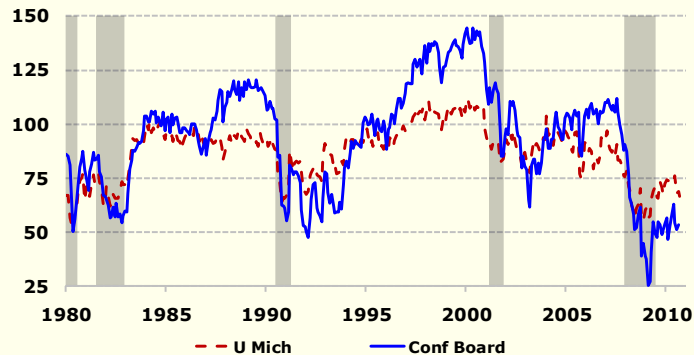


Consumer confidence remains uncertain

Index

Mich: 1966Q1 = 100, SA

Conf Board: 1985 = 100, SA



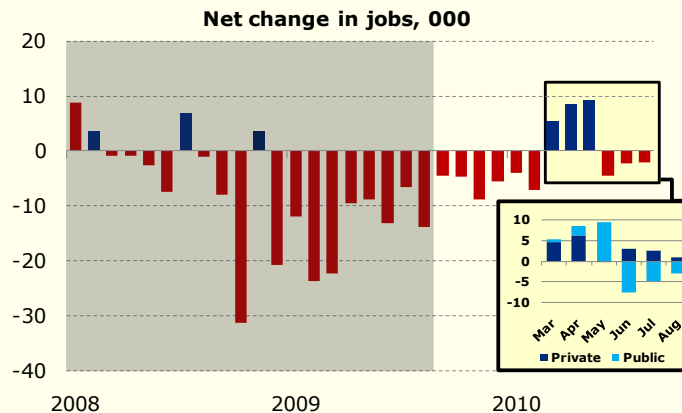
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Source: University of Michigan; Conference Board, data through September 2010

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Private sector job growth in WA mirrors the national pattern – weak and hesitant



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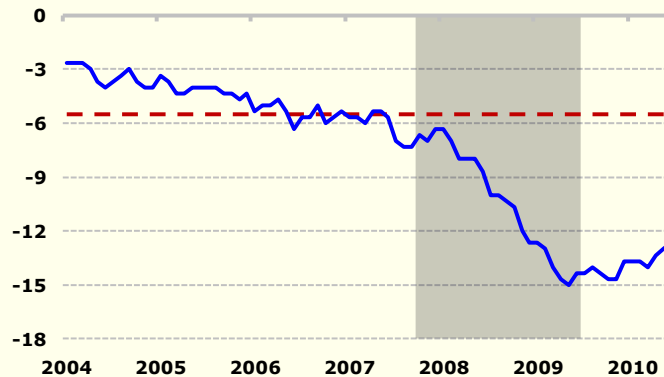
Source: WA ESD, ERFC; data through August 2010

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Credit conditions for small business are improving, but remain tight

Availability of Loans
Net Percent ("Easier" minus "Harder"), 3mma



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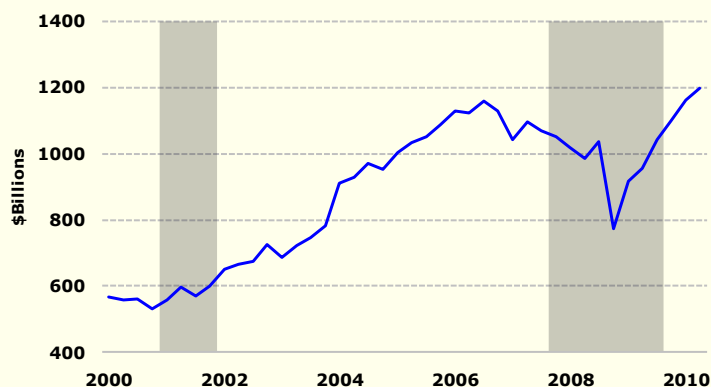
Source: National Federation of Independent Business; data through August 2010

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Corporate profits are back up above pre-recession levels

After Tax Corporate Profits, with IVA and CCA



IVA:
Inventory
valuation
adjustment

CCA:
Capital
consumption
Adjustment

With IVA &
CCA, implies
profits from
current
production

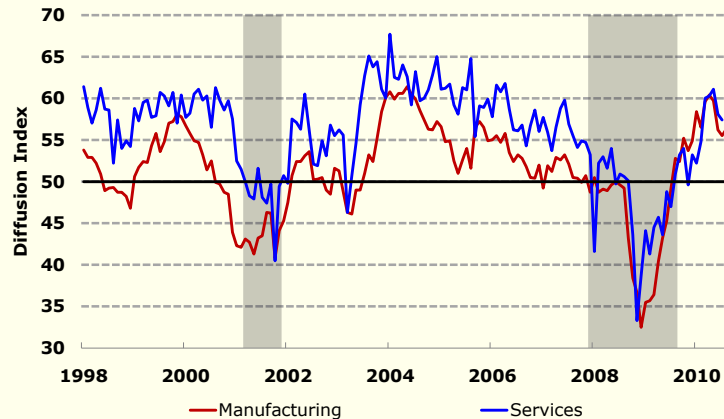
Source: BEA; data through 2010 Q2

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ISM indices for both services and manufacturing indicate moderating growth

An index greater than 50, implies growth



Source: Institute of Supply Management; data through August 2010

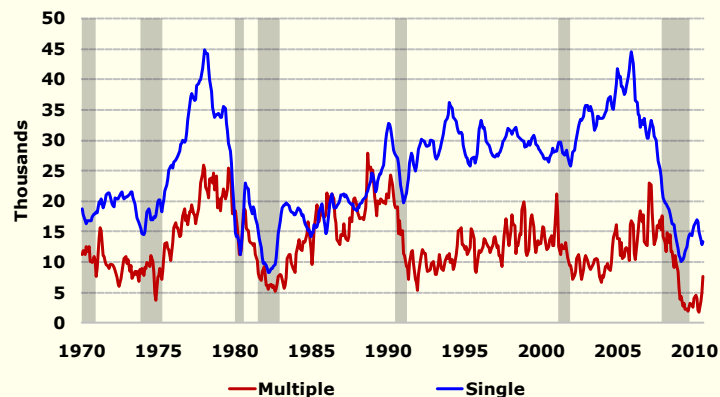
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WA building permits grew briefly from federal tax credits but remain low

Washington Housing Units Authorized by Building Permits, 3MMA, SAAR



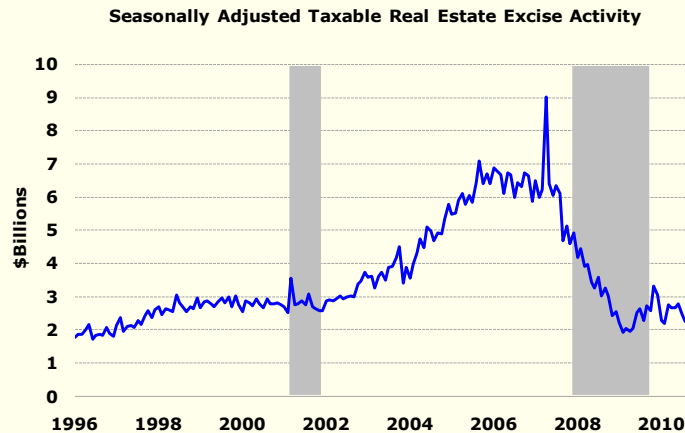
Source: U.S. Census Bureau; data through August 2010

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Real estate activity is on slow upward trend despite credit-related swings



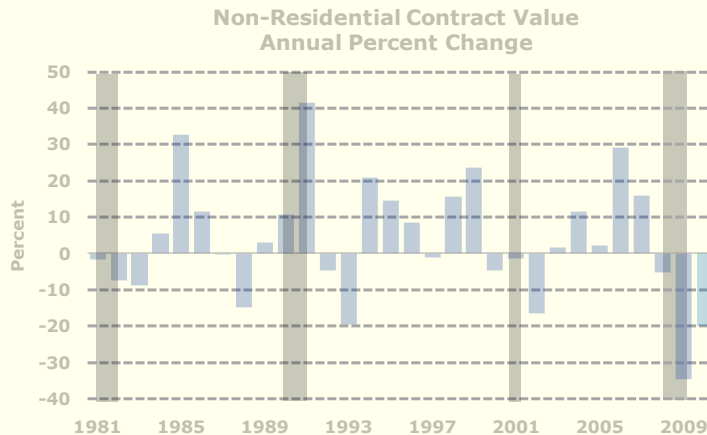
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Source: ERFC; monthly data through August 2010

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This is WA's worst downturn in non-residential construction in 30 years



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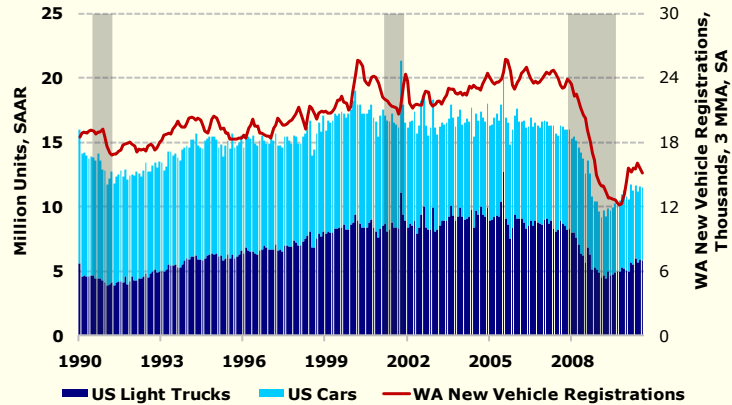
Source: McGraw-Hill Construction, data through August, 2010

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Automotive sales are treading water, after recovering from trough

Cash for Clunkers effect removed



Source: Autodata Corporation, WA DOL; data through August 2010

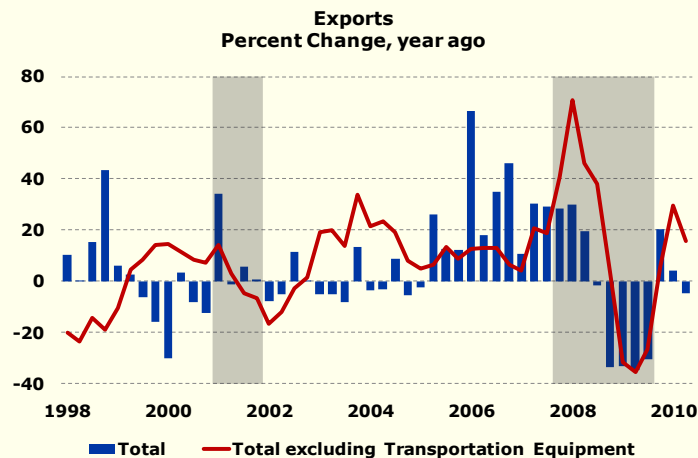
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WA export growth is slowing, but will help state outperform in the recovery

Exports excluding transport equipment were up 15.6% y-o-y in Q2



Source: Wisner Trade Data; through 2010 Q2

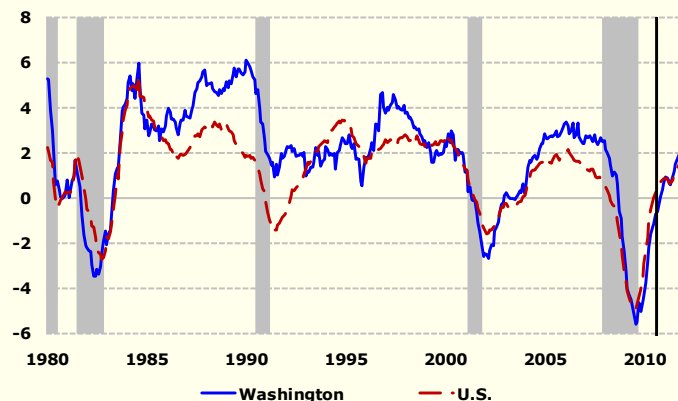
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WA employment lagged the nation in the downturn and will recover at about the same rate as the nation

Percent change, year ago



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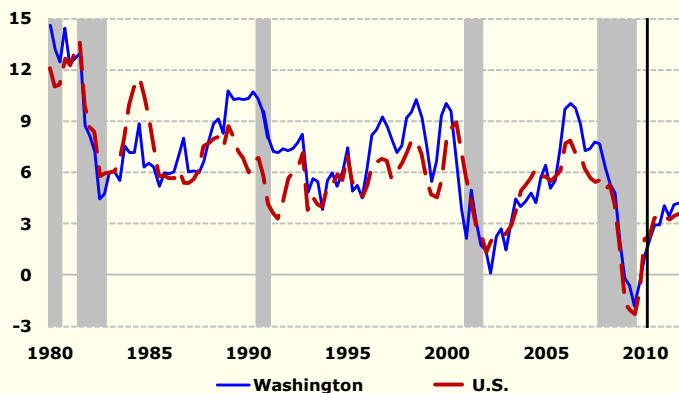
Source: ERFC September 2010 forecast; actual through August 2010

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The recovery in WA personal income growth, however is expected to be modestly better than the nation's

Percent change, year ago



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Source: ERFC September 2010 forecast; actual data through 2010Q2

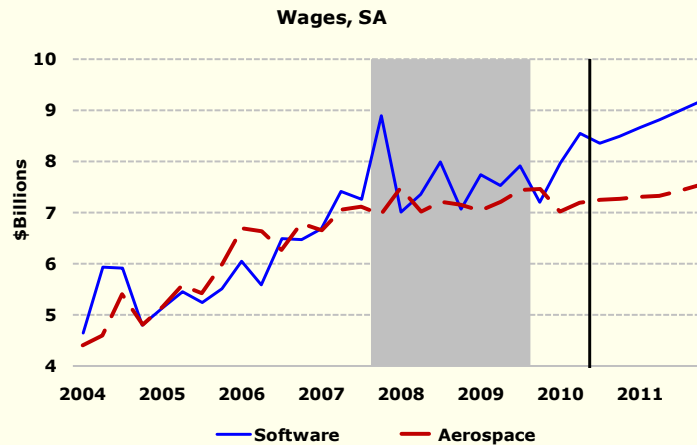
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WA aerospace and software sectors are expected to add \$4 billion in wages through 2013

Through 2013, WA aerospace and software industries will contribute 14% of wage growth, although they represent just 5% of the workforce

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Source: ESD, ERFC September 2010 forecast; actual data through 2010Q2

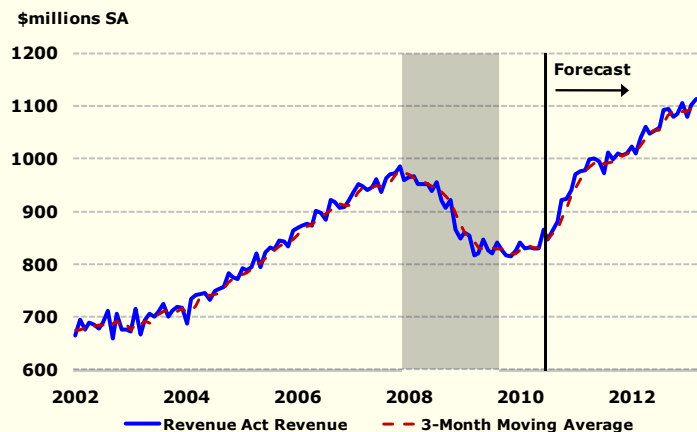
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Revenue Act collections are now trending upward, and likely to continue

Adjusted receipts were up 3.2% year-over-year in the August 11 - September 10 collection period - for July activity.

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* Adjusted for large one-time transactions, current definition of Revenue Act

Source: DOR and ERFC; monthly data through July 2010 activity; September 2010 forecast

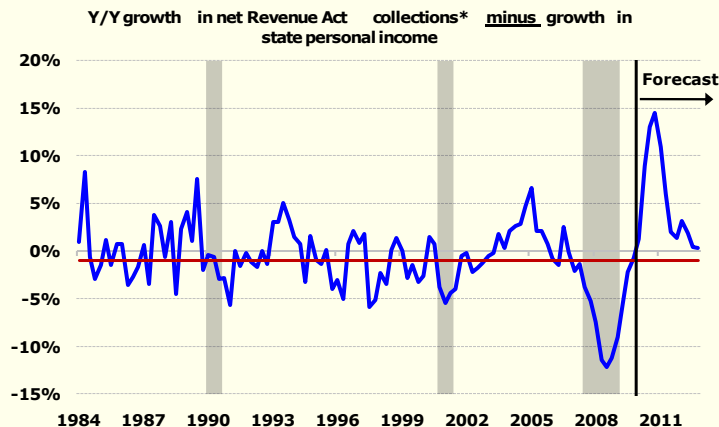
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Revenue growth relative to income will improve sharply due to 2010 legislation

The growth rate for FY 2011 is accelerated by legislative additions to B&O and retail sales taxes

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*Current definition of Revenue Act, includes effects of 2010 legislation

Source: DOR and ERFC; data through 2010Q2 estimated, September 2010 forecast

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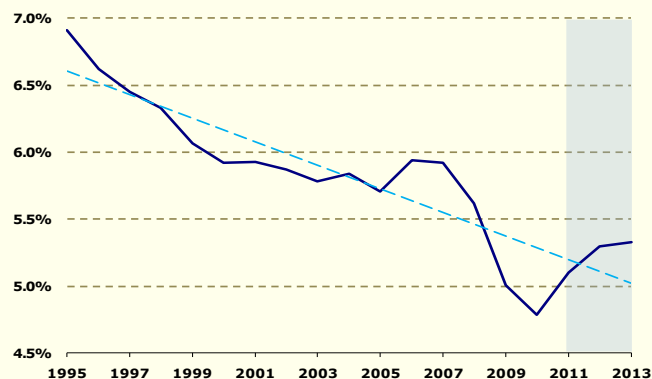
FY 2010 General Fund revenue as a share of state personal income was at its lowest level in recent history

General Fund revenue as a share of personal income has been trending downward for years.

Revenue-enhancing legislation from the 2010 session will increase the General Fund share above the downward trend in FY 2012 and 2013

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General Fund-State* Revenue as Percentage of State Personal Income



*Current definition of General Fund-State. Shaded area indicates forecast.

Source: DOR and ERFC; FY data through FY 2010; September 2010 forecast

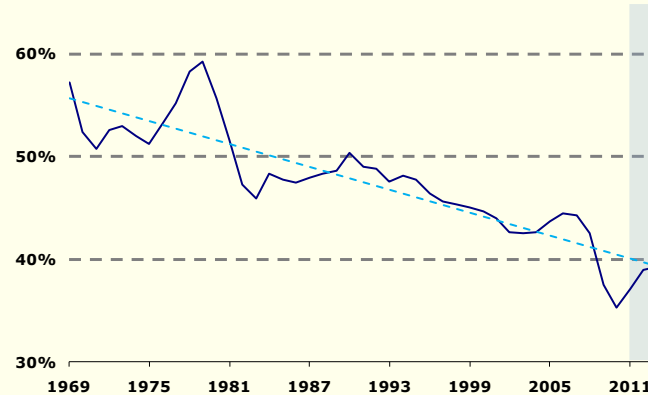
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Taxable sales make up a declining share of state personal income

The September forecast only brings sales as a percentage of income up to its declining trend line by FY 2013

Taxable Retail Sales as Percentage of State Personal Income



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*Past tax base adjusted to represent current base. Shaded area indicates forecast.
Source: DOR and ERFC; FY data through FY 2010; September 2010 forecast

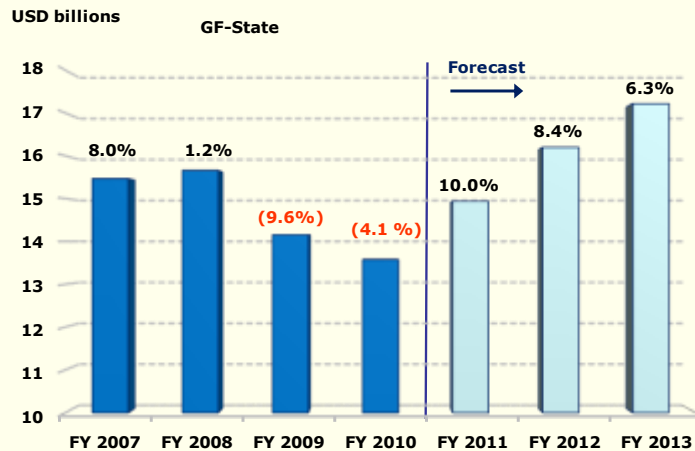
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General Fund* forecast by fiscal year

* General Fund & Related Funds for FY 07, 08, and 09

General Fund – new definition, for FY 10-13



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Source: ERFC forecast, September 2010; includes impact of legislative changes

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Forecast changes: General Fund State, 2009-2011 Biennium

**June
Forecast:**
**\$29,282
million**

**USD
millions**

September '10 Forecast

	<u>Collection Experience</u>	<u>Non- economic Change</u>	<u>Forecast Change</u>	<u>Forecast</u>	<u>Total Change*</u>
Dept. of Revenue	(\$189)	(\$5)	(\$552)	\$27,055	(\$747)
All other agencies	(\$2)	\$0	(\$21)	\$1,457	(\$23)
Total GF-S	(\$192)	(\$5)	(\$573)	\$28,512	(\$770)

* Detail may not add to total due to rounding

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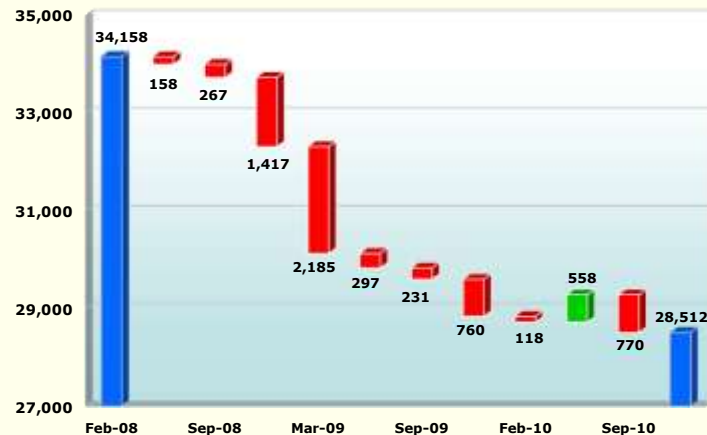
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Forecast revisions to the 2009-11 biennium

The September forecast is \$1.62 billion (5.4%) lower than the March 2009 forecast, which was the basis for the initial 2009-11 budget.

\$Millions



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Source: ERFC; data through September 2010 forecast. Current definition of General Fund-State

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Forecast changes: General Fund State, 2011-2013 Biennium

USD Millions

USD millions	June 2010 Forecast	September '10 Forecast			
		Non-economic Change	Forecast Change	Forecast	Total Change*
Dept. of Revenue	\$32,433	(\$10)	(\$611)	\$31,812	(\$621)
All other agencies	\$1,650	\$0	(\$48)	\$1,602	(\$48)
Total GF-S	\$34,083	(\$10)	(\$659)	\$33,414	(\$669)

* Detail may not add to total due to rounding

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2009-11 Biennium alternative forecasts – cash basis

\$Millions	2009-11 Biennium	Difference From the baseline
September 2010 Baseline (65%)	\$28,512	
<u>September 2010 Alternative Forecasts</u>		
Optimistic (10%)	\$28,888	\$375
Pessimistic (25%)	\$28,078	(\$435)
Probability Weighted Average	\$28,441	(\$71)
GCEA*	\$28,575	\$33

*Based on the Governor's Council of Economic Advisors' assumptions

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2011-13 Biennium alternative forecasts – cash basis

\$Millions	2011-13 Biennium	Difference From the baseline
September 2010 Baseline (90%)		
\$33,414		
<u>September 2010 Alternative Forecasts</u>		
Optimistic (5%)	\$35,845	\$2,430
Pessimistic (5%)	\$30,597	(\$2,817)
Probability Weighted Average	\$33,395	(\$19)
GCEA*	\$33,319	(\$95)

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*Based on the Governor's Council of Economic Advisors' assumptions

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Conclusion

- The forecast for the 2009-11 Biennium is \$770 million lower and the forecast for the 2011-13 Biennium is \$669 due to a weaker economic outlook
- The economic recovery is going to be a slow painful slog, and it is difficult to see what is likely to cause growth to accelerate
- Both the downside risk to the forecast, as well as the level of uncertainty in the baseline is significantly higher than in June

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